Background Document on Financial Framework Review

Informal Consultation

24 April 2014

1. Following the discussion at EB.1/2014 on "Financial Framework Review: Working Capital Financing", a follow-up informal consultation was held on 2 April at which:

    A. The Secretariat outlined the conceptual framework for a comprehensive approach to the Financial Framework Review focusing on improving operational efficiency and effectiveness through three components:

        i. Predictability
        ii. Flexibility
        iii. Accountability.

    B. As part of the predictability component, The Boston Consulting Group (BCG) presented preliminary recommendations from their pro-bono review of the Working Capital Financing Facility (WCFF). BCG emphasized that the existing advance financing framework covers three very diverse needs, each with distinct risks: internal lending, pipeline management and capital financing. BCG indicated how it would further analyse data to finalize its recommendations.

2. Participants at the informal consultation appreciated the approach to be used for the Financial Framework Review and welcomed the ongoing BCG review. It was suggested that an additional consultation on the WCFF proposals be held in advance of EB.A/2014.

3. Based on further analysis undertaken since early April, this document outlines the Executive Board decisions that will be described in more detail and presented on 24 April and – subject to that discussion – confirmed in the documentation to be presented at EB.A/2014.

4. These draft decisions are as follows:
   The document to be presented at EB.A/2014 will describe the overall objectives and goals of the Financial Framework Review, its three components, and the outline of the process to be followed in conducting the review.

Draft decision (i) would thus state: "*The Board welcomes the comprehensive approach to the Financial Framework Review outlined in [TITLE OF DOCUMENT] [number].*"

5. The document to be presented at EB.A/2014 would explain in detail that there are effectively three different facilities currently operating within the current 'Working Capital Financing Facility': internal lending for project operations; pipeline management provided by the Forward Purchase Facility; and capital financing provided by Corporate Services advances. These three different facilities have different objectives, different modalities and different risks. The risks will be described and quantified.
   The Secretariat believes that treating the three facilities separately in future will increase transparency and accountability and significantly strengthen governance.

Draft decision (ii) would thus state: *"The Board approves the separation of the Forward Purchase Facility and Corporate Services advances from the Working Capital Financing Facility."*

6. The initial BCG review presented on 2 April indicated that no dedicated reserve would be needed for the Forward Purchase Facility. Nevertheless, the Secretariat will propose the establishment of a small, dedicated safety net of last resort for the Forward Purchase Facility, to be funded by a transfer from the Operational Reserve.
Drawing on BCG's detailed analysis, the Secretariat will describe and quantify the minimal risks faced by the Forward Purchase Facility. Specifically, the documentation will explain how the risks are currently mitigated, including through WFP's Self--Insurance Fund and quantify the very limited residual losses incurred to date.

Draft decision (iii) would thus propose: *"The Board approves the establishment of a reserve for managing Forward Purchase Facility*[1] *losses and the transfer of USD 6 million from the Operational Reserve to the newly established Forward Purchase Facility reserve.*"

7. On the assumption that decisions (ii) and (iii) above are approved, the remaining Operational Reserve balance will be USD 95 million, which will be used exclusively as a reserve of last resort for internal lending.

8. Further analysis from BCG indicates that the current leverage ratio of 6:1 for the WCFF authority (USD 607 million) to the Operational Reserve balance (USD 101 million) could be significantly increased to manage the risks associated with internal lending. BCG's analysis also proposes an increase in the internal lending ceiling to USD 630 million. The Secretariat will propose a continuation of a more conservative and therefore larger Operational Reserve balance and a more conservative internal lending ceiling of USD 570 million.
The risk analysis and rationale for the internal lending ceiling will be described in the document to be presented to EB.A/2014. The need for increasing the internal lending ceiling, which currently effectively stands at USD 207 million, and the criteria for expanding internal lending judiciously, will also be described.

Draft decision (iv) would thus propose: *"The Board approves the ceiling of USD 570 million for the Working Capital Financing Facility to be used for internal lending for project operations."*

9. The current WCFF authorization of USD 607 million includes USD 350 million dedicated to the Forward Purchase Facility. The proposed amount will remain unchanged, although an authorization will be sought for a separate, stand alone Forward Purchase Facility in line with draft decision (ii).

Draft decision (v) would thus state: *"The Board approves a threshold of USD 350 million for the Forward Purchase Facility."*

[1] Consideration is being given to renaming the Forward Purchase Facility as the Pipeline Management Facility.

10. The current WCFF authorization of USD 607 million also includes USD 70 million earmarked for Corporate Services advances – including the Global Vehicle Leasing Programme and the Capital Budgeting Facility.
    The proposed amount will remain unchanged, although an authorization will be sought for a separate, stand alone Corporate Services facility in line with draft decision (ii). It is also proposed that the regular review of this decision become part of the Management Planning process.

Draft decision (vi) would thus state: *"The Board approves a ceiling of USD 70 million for Corporate Services advances for 2014 and looks forward to reviewing this regularly as part of future Management Plans."*

11. As outlined on 2 April, the analysis indicates that no dedicated reserve is required for Corporate Services advances.
    However, in the unlikely event that expenditure is incurred that cannot be funded from other sources, the PSA Equalization Account (PSAEA) is proposed as a reserve of last resort. The Board would be asked for specific authorization on a case by case basis before the PSAEA could be used. This will strengthen transparency and accountability over management's stewardship of capital expenditure.

Draft decision (vii) would thus state: *"The Board takes note of the intent to use the Programme Support and Administrative Equalization Account as a reserve of last resort for Corporate Services advances."*

12. The final decision acknowledges that further discussions, both formal and informal, will take place on the various components of the Financial Framework Review.

Draft decision (viii) would state*: "The Board looks forward to further discussions on the Financial Framework Review as outlined in this document."*